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PARTICIPANTS:	Eric Rohr Dan Foster Darren Stumberger Michael Hild
ABBREVIATIONS:	(UI) = Unintelligible ***** = portion of recording redacted

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DARREN: I mean, there's two things we need to dissect here. One, what have rates done this month, and I think, Dan, you're getting close to having that finalized. What have rates done against the portfolio and the magnitude of all the variables? That's one. Number two, all of the moves in marks and all of the gymnastics, what has that caused? You know, what effect has that caused? Leading up to this month was around (U/I) basis points around there, 82, so that's the drop in the basis that we've seen. (U/I) so I just need to see

all these different variables weighted against each other.

MICHAEL: So I suspect that what you guys are gonna find once you've dissected this is that two massive negative things happened. The basis changed like you just described which, call it 20 million plus by itself in isolation, and then I guess number two is the updated static rates which are now 25 basis points higher, right?

DARREN: Yeah, I mean, that -- those would both be negatives to the portfolio. But Dan, I mean, do you want to get into, you know, what we did to IDC marks, the MACRs and all of that? Does any of that play into this or no.

DAN: It's a seemingly simple question that -- it does play into this. For instance, the -- I'm pulling it back up now. That's, for instance, in number -- in Scenario 1, that's -- the MACR is why you see a positive 20 million mark-to-market gain, so it does play into that. It's a simple question, but it's not really a simple answer. Scenario 1 is supposed to be just

getting back to whatever was in IDC at February month end, but because of the MACR situation, it led to the $20 million gain.

MICHAEL: Okay, so meaning the MACR situation meaning how we had to move things off of Wedbush and into different locations at higher haircuts and the like, so the $11 million impact that's being shown here is already accounting for something that we've -- we already knew about and already did or is this something new that's on top of what we understood to be the case before?

ERIC: I think, so when we -- you know, we just ended up, keeping our February marks in total flat to January, like just recorded no mark-to-market gains in February. I think, Dan, correct me if I'm wrong, is underneath I said, hey look, when we go to sell that big MACR in March, it could look like it's being sold at a huge loss, so mark it down effectively and then remark the things to offset it.

DAN: Exactly.

ERIC: So we have no realized gain or losses when we sell it because otherwise it's gonna look really weird, like you had it marked here at the end of February –

DAN: Yeah.

ERIC: -- and then you sold it at like $12 million loss effectively, even though -- but then the IO that got separated had a huge gain, so you didn't correct for down the line; you just remarked the MACR back up in essence and reversed that. Is that correct?

DAN: Yeah, yeah. So said a little bit differently is if we didn't do anything, just conceptually it would be a $19 million loss on the MACR, but you get a $19 million gain on the underlying IO.

ERIC: Right.

DAN: Okay, that's great. But we didn't want to take that loss on the -- when we sold it to Nomura, so we just marked down the MACR, marked up the rest of the position, but now when we sold the

MACR, there's no mark-to-market, but we're still taking back the IO and then marking it up to 19 million because we already own that bond, so it doesn't offset anymore.

ERIC: Right. Understood.

DAN: Yeah.

[OVERLAY]

ERIC: A simple question.

DAN: Yeah.

ERIC: Kind of a nuanced answer.

DAN: Yeah, and you were asking about the 11 million down in liquidity. It's -- I -- some of the answer -- this is what I was looking on before we hopped on the call. Some of the answer is we -- the mark-to-market right now, we borrowed some -- what I think the answer is, we borrowed some using the updated IDC prices I believe, and --

ERIC: Yes. That's exactly what happened.

DAN: Yeah, and if we mark everything back down, then it's --

ERIC: You've got to give back that money.

DAN: Yeah.

ERIC: Yep.

DAN: That's what I think the answer is. I'm not saying we want to do this or should do this. One scenario I didn't quite have time to prepare is we could look at it -- we could do this another way where we reverse -- we could do it, I don't want to say smarter because smarter's not the right word, but write down certain bonds that wouldn't have liquidity impact to offset that positive 20 million and not have a liquidity impact such as Nomura.

ERIC: More sophisticated, refined, is what I think you're –

DAN: Yeah.

MICHAEL: So is the 77.2 number, what's magical about that number? Is that, you know -- it's basically you're just saying you solved for what the prepay needed to be to get back to that February number?

DAN: That's correct. Yes.

MICHAEL: Okay, I see.

DAN: Oh, you know what? That's – I think I know why it's lower than we expected. It's because we -- in order to write down the MACRs, I had to write up the other bonds, so it's not an apples-to-apples comparison. When it says February month end, it's not to the same prices as when we ran it to February month end at the end of February.

ERIC: I'm not sure I follow, Dan, completely but I think I understand a little bit.

DAN: Yes. So the last time that we ran the 92 percent is when we didn't touch any of the MACR pricing, nothing with that, so the prices -- forget the MACRs for a second. For all the non-MACRs, the

things had a price, and we ran it, and it came out to 92 percent. Now we redid February month end, the difference being we raised prices 20 -- yeah, we raised the non-MACR prices 20 million to offset the loss of the MACR, so all else being equal, you're running higher prices for the other bonds, and then on top of that, you have the 20 plus million issue from basis contracting, so it's -- that's what the difference is.

ERIC: Okay, I didn't follow all that. We may need to lay that out.

DAN: Yeah, it's not trivial, but I'm happy to take a stab at writing it down or sending it in an email, but I think that's what the explanation is. It's not -- said a little bit differently, you're not only running it slower because of the contraction in basis. You're also running it slower compared to when we ran it on the 92 percent because the prices are now higher for those bonds because we changed them to offset the MACR being sold to Nomura, so I think it's a combination of two of those things.

ERIC: I mean, part of this, you know, we need to make a decision, and I'm just being ultra candid here, is we certainly can't mark up the portfolio anymore. Well, not we can't. We should try to avoid it if we can right now just because it's just getting farther and farther away from reality, I guess, or the center of the universe.

[BACKGROUND NOISE]

MICHAEL: So did -- so am I correct in making a statement that part of what's impacting Scenario 1 and scenario 2 is the change in static rates that occurred this month?

DAN: That's certainly material change.

MICHAEL: Can you identify the amount of materiality that that was?

DAN: Yes, I actually have that. One second. So as of 3/22, it was -- just the basis was 27 million.

MICHAEL: Well, if you –

[OVERLAY]

DAN: I don’t want to overcomplicate it, but just to be clear, it was 27 million undiscounted, but that was just basis. Rates, I don’t think, have been favorable, overall.

DARREN: Well no, I mean, like I’m saying is you had this quarter point raise so that -- with rates being 25 basis points higher, that by itself -- you know, in the static scenario, obviously it causes faster buyouts when you go up 25 basis points in rates.

DAN: Yeah, I mean, that’s certainly a piece of it, too.

DARREN: You would just have to run the portfolio current, one month, one year, and then subtract 25 basis points and run it to see what the (U/I) in the market value is to get the magnitude. That’s what the question is.

MICHAEL: Well, whatever it is, I know the Fed rate is just like 25 (U/I). I don’t know what the actual static rate was. I mean, was it exactly 25 BPS or was it something, you know, closer to –

DARREN: I'll take a look. I've got that somewhere, too.

DAN: So in the month of March, March 1st you started at -- well, when did you run month end for February?

DAN: Yes. That's what I'm trying to pull up now.

DARREN: I've got the 20th where monthly was at the –

DAN: Yeah, 77, 78, that year, annual was at 1.73. That basis was .96.

DAN: So February 20th (U/I) the LIBOR was 77. Today it's 98, so basically 20 basis points.

MICHAEL: I guess we're-- I'm curious what the impact is –

[BACKGROUND NOISE]

DAN: I can run that.

DARREN: What I would do, Dan, is to see the relative effect, you want to keep the basis constant and just let's figure out what the effect of the 20 basis point move by itself is on the portfolio, and then it would be nice to see, okay, then you control for basis, so you know, the question would be what is a 20 basis point, you know, effect on the portfolio, question one. Question two, what is a, what did I say it was, we're saying it's 82, 96 -- what is a 16 basis point, basis contraction effect on the portfolio? I think that's the root of what we're trying to figure out. So it's do 20 and then 16?

MICHAEL: To be clear, whatever it was, right? So you've got the raw data in terms of what the basis contraction was and what the actual change in static rates were for both one-month LIBORs and annual. We own both. So whatever it is, let's get the raw numbers and solve for it.

DARREN: Okay.

MICHAEL: I think what Darren's saying is 20 basis points is, you know, is in loose terms is

what he's saying is approximately what it was, but let's look to see exactly what it was for each of those two and calculate what the exact change in rates was in isolation and see what the impact of that is, and then whatever the basis contraction change was, you know, run that in isolation so we can (U/I) that part –

DARREN: What the rate effect was, what the basis effect was. I can help you after this call, Dan.

DAN: Okay. Then maybe it's for after this call, but how should we price it because scenario 1, you saw your given price. Should it be like scenario 3? Because like in scenario 1 and 2, you're given a price, so I need to know how we want to price it.

[OVERLAY]

MICHAEL: Pick a scenario.

DAN: Okay, and just keep -- okay, yeah, that's what I was thinking.

DARREN: I mean, let's look at the relative move in market value with a starting set of prices.
DAN: Use Scenario 3.

DARREN: Yeah, understood. And I'll do it since previous month end, I would think, or when I ran last liquidity. Which one do you want to use?

ERIC: Well, I think for your gap numbers, you run it against, you know, obviously where the marks currently are, right, and then for liquidity you run it against the last liquidity.

DARREN: Well, the last liquidity was a couple of days ago which is kind of a base question.
ERIC: Which liquidity did you run? I mean, you and I already had this exchange. Did you ask Annie -- the one we showed Michael, basically –

DARREN: Yeah. That was 3/21.

ERIC: Yeah, so there's been no other liquidity since that one.

DARREN: Okay.

MICHAEL: I mean, my concern, you know, just stating it out loud is that, you know, we took hedges off because they're not producing any benefits. It's just downsizing it seems like, and with that having been said, you know, the four grade curve already reflects two -- you know, it's already predicting that the fed's gonna raise rates, right, throughout the year, so there's nothing we can put on in the form of a hedge to protect against that, and like you know, I mean, it's stating the obvious, my concern is if we're saying, hey, look, every 25 basis point shift there's like a $40 million hit to the portfolio or, you know, some massive number, you can only lower prepays but so far. Your debt, right, you're out of ammunition, and so if we're saying those two more rate increases, were they to occur this year as planned, were to happen, then you know, we've got a massive issue on our hands because if it's -- it's one thing if it's the basis that's causing this degradation. It's another thing if it's the rate. If it's the rate that's causing it, then you know, that's a real

problem, right, because, I mean, to stretch a point to make a point, you can only go from prepays from 57.2 to 0, right? You can't go negative, so I mean you can only go but so far.

DARREN: It's going to be predominantly in the basis, without a doubt. This was a massive, massive movement of the basis that happened really quickly.

MICHAEL: Again, driven by the Fed rate increase, right, because, you know, the Fed has basically said yeah, we're gonna jack up rates, damn the data, so now's the one year and the one month spread contracted considerably because longer term rates are not moving up at the pace that short term rates moved up, and so the discrepancies between one month and one year, so that the gap between those two contracted massively because the fed's artificially raising short term rates higher than what they should otherwise be. Do I have that right or is it something else –

DARREN: These are all considered like -- most are short term rates, even if it's 136 one year.

They tend to move lockstep, and there's weeks at a time where they, you know, I could pull the charts. They move -- unless there's some kind of financial crisis, they move lockstep. However, when there's Fed meetings and a lot of that, it takes -- it could take up to a couple weeks to completely normalize so you've had one month that's shot up. One year really hasn't budged. Now, the expectation is one year is gonna to kind of catch up over the next period of time, but, again –

DAN: Or it's not because I'm right and Janet's smoking dope.

DARREN: Yeah, I mean, the basis has gone one way since we've started here, and it was wider, and this is like the first time it's kind of coming off of those highs.

MICHAEL: Yeah, I understand what you're saying, but I mean, I think there's some element of, you know, the forward curve won't cooperate with what Janet's trying, you know. She's got her agenda to raise short term rates, but the rest of the curve isn't moving at the same pace because people

don't believe, you know, inflation and GDP growth and long-term growth is, you know, keeping up with the pace at which she's forcing rates to be raised in the short term. So even if it's the difference between one month and one year, I mean, I think there's some legitimacy to that argument even though it's on the short end of the curve, but I understand what you're saying. Still, one year short term rate, but unfortunately for us, you know, an inverted yield curve will probably still create this problem even in that gap between one month and one year were it to ensue because it's not just, you know, 5, 7, 10, 30 year money that's going to drop like a stone. It sounds like there's gonna be, you know, there's gonna be a contraction between one month and one year, so hold onto your, you know, hold onto your seat. I don't know. I mean, Darren, maybe you feel differently. You feel like the one-year curve's -- one-year rate is -- this is gonna normalize in a couple weeks' time?

DARREN: Yeah, I -- unless there's kind of these shocks (U/I) shock to the system, I

wouldn't expect, you know, the basis to continue to contract. I would expect it to catch its breath and normalize. That's my expectation. I mean, I'll look more into it.

MICHAEL: Yeah.

DARREN: I mean, everything is quiet as it can be in kind of the leading signals. Obviously, the curve has flattened and that's a refreshing predictor. I get it, but you have, like all the other things, like the spreads between three month LIBOR treasuries, the spread between three month LIBOR funds, OIS, all of that is sitting at like -- if you look at the fix is at 12. Everything is sitting at ultra, ultra-complacency levels as if there's nothing expected at all to happen bad. It's just what the numbers are showing. I think the backend is gonna stay pegged until DC can figure out what the hell they're going to do, what they can pass, so I think the back end is still saying okay, prove to me there's growth. Prove to me there's inflation. I'm not gonna break through G60 until that's proven. What are -- what is Congress gonna pass? Until that happens, we're not budging

through G60. We're gonna stay in this range between 230 and 260. On the front end, obviously you have the Fed pressures, so you have all the knucklehead Fed governors come -- see, what's happening here is the Fed governors are coming out intra meeting and saying they're gonna hike 2, 3, 4 times, and what happens is, in anticipation of Janet, and people thought that she would kind of continue that spiel, she came out dovish and that was the big retracement. So I don't know what game they're playing, but now it's a trend. The Fed governors are coming out every day and saying they need to go higher -- you know, 2, 3, 4 times this year, definite, has to be, and then by the time -- so then the market's gonna price in the Fed move and I guess June is the next one, and then she's gonna come out and be dovish again. So it's like -- it's a lot of games being played.

DAN: She's been kind of dovish after she's raised the rates again despite the –

DARREN: Yes, yes. Yeah.

DAN: -- and we get screwed.

DARREN: Right, so the market's gonna be selling off, selling off, selling off into the meeting, and then she's gonna come out dovish, and then you're gonna rally back. I mean, that's been the trend now. It's like her minions are doing the dirty work by causing rates to go up.

MICHAEL: Yeah. So I guess what -- the nature of my question, again, is trying to disentangle static change -- the change in static rates, call it 20 BPS, whatever it is, what the impact of that was as compared to the contraction of a basis or a scenario that's already shown here. Nothing else changes, so you know, use, I don't know, pick scenario 3, as an example, right? We're saying there's a $43 million, $44 million impact to liquidity, $23 million impact to marks, mark-to-market, tell me how much of that was related to basis contraction versus a rise in static rates.

DARREN: Yep.

MICHAEL: I mean, Eric, tell me if you disagree, but that's what I'm trying to get a sense for, is just not changing anything else and using one of these scenarios here that are on the page to be able to tease that out, and I'm gonna hope that it's, I'm gonna hope that it's more basis than it is static rate increases. If it's static rate increases, there's absolutely not a damn thing that we can do.

ERIC: Yeah, I agree with the approach to tease that out and the importance of teasing that out.

MICHAEL: I mean, the only other thing that you're left to assume is that, you know, in your forecast is that -- what do we assume, like this basis in our forecast, do we take the current basis as it stands and then project that going forward into the future? So in other words, if it contracts by 20 BPS, let's just use that as an example, do we then assume that that 20 BPS contraction is going to continue into perpetuity?

DARREN: Well, we assume, you know, if you take -- you're writing a portfolio at a snapshot, so

it would assume that the basis doesn't move from here.

MICHAEL: Ah.

DARREN: It doesn't normalize. It doesn't get any better. It doesn't get any worse.

MICHAEL: Got it, because it's taking the whole concept of whatever the forward curve is out of the mix and simply saying static is this, the rates are this, assume they're gonna stay this into perpetuity, so both basis -- both the absolute level of rates as well as the basis are going to continue in both scenarios 1 and 2, you know, for as long as the eye can see –

DARREN: Yes.

MICHAEL: -- and then it's simply the prepay that's being adjusted.

DARREN: Yep. Correct.

MICHAEL: Ah. I understand. So it sounds to me like the only thing that or the only items that are really out there that are on the table,

and I'm not saying any of them are used, but just saying the only things that are really on the table for consideration are what do you assume for prepays, what do you assume going forward for the basis spread between one month and one year, and what do you assume for the purposes of rates? Is it static or is it something that's changing over time? I mean, those are really the only bullets left in the holster, I guess, as it pertains to assumptions.

DARREN: Yeah, that sounds right. Yeah.

MICHAEL: Yeah. So of the lot, you know, I'm just talking off the top of my head, of the three that were just described, the one that, well, I don't like, you know, monkeying with any of these, but you know, the one that, to me, if Darren's right, the one that seems the most defensible and/or reasonable, I don't know what the right word is, maybe reasonable is the right word, I wouldn't even use the word defensible. I guess you'd just say reasonable, the one that's the most reasonable to make some form of an

adjustment to would be to -- would be that spread to say, look, we're not going to assume that this moment in time of this contraction that just occurred is going to continue for the next, you know, 11, 12 plus years. You know, we're going to assume something different so that it normalizes, but I don't know, just talking off the top of my head, but the other two, you know, I would say -- I can't sit here with a straight face and say given what Janet Yellen's doing that I would expect that short term interest rates are going to go down, and I'm having trouble with the argument that prepay fees are going to slow given all the craziness going on in the refi world which I guess I understand to be what's the cause of prepay fees coming in higher than what we want. I don't know. I haven't seen the analysis on that, if it's really disentangled exactly what's causing the rise in prepay fees that we're observing--whether it's that or whether it's these artificial pull buyouts, optional pull buyouts like we did with EverBank that are causing it, that others are doing, or whether it's something else, but nonetheless, I guess just hanging my

hat on the HECM-to-HECM rebuy activity and assuming that that's the predominant cause, you know, I will tell you while I'm working on it, man, it's slow to try and get NRMLA and the broker dealer community to act in order to stop the nationwide securities of the world from just continuing to do what they're doing. I mean, I'm still hopeful, but is that gonna happen, you know, next month? No. Is it gonna happen this year? Maybe. You know, is there a possibility that nothing happens, and we can't reign these guys in because we can't force all the broker dealers to honor NRMLAs rules? I think there's a chance. All it takes is one to provide liquidity to these guys, and they're gonna continue, you know, continue violating the rule because that's kind of how they've built their business. So, I don't know. I'm just talking out loud. There's nothing really to say there. I'm just making an observation, so -- Eric, do you have anything you want to add?

ERIC: No. Can we drop rates to negative?

MICHAEL: You mean like everywhere else in the world except for here?

ERIC: Yeah. All right.

MICHAEL: Well, it is what it is. So -- all right, well, if you know, for grins, Dan, if you can disentangle, I guess for scenario 3, what, you know, what the basis versus data grade impact is for both liquidity and marks, I'd appreciate that, and then, I don't know, for grins, Darren, you know, I don't have a whole lot of context here about what normal is in terms of, you know, the spreads, basis spread between one month and one year, but you know, it might be interesting to see that if we say things are going to normalize and the impact was call it 20 basis points, if that 20 basis points, you know, normalizes after a month, you know, how does that change scenario 1 and scenario 2?

DAN: Or normalize to where it's been pre-March? I mean, I have the graph -- I have the 1-month/12-month graph, and it'll be interesting, I'd like to get your perspective on it. Here, let me just find it.

MICHAEL: You're probably gonna tell me that we're like at all time wides or something like that.

ERIC: Very close to it.

MICHAEL: Oh, wow.

ERIC: I've seen the graph, yeah.

MICHAEL: All right, I just opened it up.

DARREN: Okay, so look at -- the bottom half is easier to understand. That's the actual spread, so when you see the shaded green, that's the positive spread between the two.

MICHAEL: Yeah.

DARREN: So, let's see. Wait, this is only to 2010. Wait a second. Shit. Huh. I don't know why it's going to 2010. I thought I had it for the -- I think I just sent it to you, Eric, right? Oh, this is not the right one. Hold on. Here it is. Okay, yeah. You should have it.

ERIC: Okay.

DARREN: So here you see -- what I was alluding to is look at when the portfolio was acquired 2014 all the way to the left, and that basis is just increased, you know, for the most part, and then you see that dip at the end here in March, and if you look at something historical, historical I think it's been around 50 basis points.

MICHAEL: So just to be clear I should be looking at the graph at the bottom on the left which is the spreadsheet –

DARREN: Yeah.

MICHAEL: -- showing -- yeah, in the area of -- okay, good. Yep.

DARREN: So that, you know, going from, call it 40 basis points up to 100, you know, that was probably a -- easily -- yeah, the portfolio -- if the portfolio was this size back in August of 2014, that would have -- that basis move held constant, my guess would be 20, 40, 60, 80, 80-ish, 75 to 100

million in benefit, but we'll get firmer numbers when Dan runs the isolated runs.

MICHAEL: I mean, for such a small move, you know, in the grand scheme of things to cause a $27 million end discounted impact, I'm -- wow. That is profound.

DARREN: Yeah, it's a -- and obviously, as you can see, it's been nothing but good to us. There was a period of time, I guess, looking at kind of November, December 2015 it dipped. It's dipped a few times, but –

MICHAEL: Yeah, and the reason that this has been widening as much as it has is because the market has been predicting that the Fed was going to raise rates faster than they did, and one month LIBOR remained low because rates weren't raised and, therefore, the disconnect between what the market was expecting and what was happening in reality continued to grow and grow and grow until, you know, boom. You see a 25-basis point increase, and then it contracts. Is that –

DARREN: Somewhat. I need to do more work on it. I think it has more to do with expectations, you know, not exactly what happened to 25, not the 25, but how the -- you know, they call it the dot plot, how that shifted in this meeting. You know, because all the governors basically had their own projections, and they throw that into a plot, a plot graph.

MICHAEL: Yeah, I get what happened, I guess, now. I guess what I'm trying to figure out is what happened between, call it December 2014 and you know, call it 2016, where you saw this widening over time, and then man, a drastic widening in 2016 at the beginning of the year.

DARREN: Mm-hmm.

MICHAEL: I mean, what's the -- I'm trying to get my head wrapped around what the cause of that is.

DARREN: I have to go back and figure it out.

ERIC: Yeah.

DARREN: I know a good portion of the move in 2016 towards, you know, call it -- the probably 10-ish, 8 to 10 months leading up to October 2016 was related to the Dodd-Frank changes related to money market funds in that, you know, there were new regulations and new guidelines on how money market cash is allowed to be invested. That caused the basis to widen, particularly as it relates to 3-month LIBOR, and I think 3, 6, and 12-month just kind of all moved together, and one month was pegged, so –

MICHAEL: So you're saying this runup you think might be Dodd-Frank related?

DARREN: Oh, yeah. It definitely is. It definitely is. Like that runup from looks like, I don't know, summer -- definitely the summer to October move, definitely Dodd-Frank related.

MICHAEL: You're talking summer of what?

DARREN: 2016, yeah.

MICHAEL: So last I checked Dodd-Frank is still around, so what happened? I guess why did it kind of rise and then partially contract? Is that related to the rate increase that happened December last year, so again, a corresponding drop?

DARREN: Yeah, I see what you're saying. Well, the rates were -- 'cause that would have been after December because they did it in December. Or was it September?

MICHAEL: But they probably priced it in, I guess, in the fourth quarter, call it October, November. They're like yeah, they're raising rates in December, so it's started contracting in anticipation of the move.

DARREN: The move itself will cause a gyration, but again, it's supposed to normalize -- it's supposed to take, you know, weeks to normalize, and the spread's supposed to be -- basically go back to where it was pre-move. I mean, that's what I know.

MICHAEL: Yeah. It doesn't seem like that happened, though, between -- I mean, the last Fed

increase since -- I mean, what was the last rate increase that happened? Was it –

DARREN: September.

MICHAEL: December, right?

DARREN: I think it was September.

MICHAEL: Oh.

DARREN: Let me go back. December, December.

MICHAEL: Yeah, so, I mean, the story I have in my head is boom, every time there is a -- there's a rate increase in the short term, we're going to see this, you know, impact where you see the, you know, call it a 20 basis point reduction in the spread, I mean, because it never came back, right? So it looks like it contracted in anticipation of the rate change in December and then never bounced back, right, and then just happened again, another 20 basis points, so if I'm thinking about this right, you see two massive things happen simultaneously when the Fed raises rates. You see a 20-basis point

contraction in spread, and you see a call it 20, 25 basis point increase in the static rate, and the combined effect of that is absolute total devastation on our portfolio each time it happens. So it's not just like -- I mean, tell me I'm wrong, but that's what I -- I mean, that's what I'm taking away from this is that you get hit with two things at the same time simultaneously and it's like they're almost like permanent and not -- they don't -- it doesn't seem like there's any normalization that occurs.

DARREN: Well, they raised rates in 2015.

MICHAEL: Okay. Yeah. All true.

DARREN: There's only been three rate rises since 2004.

MICHAEL: Yeah, that's a good point.

DARREN: I could -- I need to work with Marty at Wedbush who understands the gyrations here. I know the runup June to October 2016 was Dodd-Frank. I want to say I asked these questions at the time –

MICHAEL: So Darren, stop right there. I'm sorry. So you say the runup meaning like that steep increase that happens basically post-July 2016 or are you saying the runup, you know, all the way up to that point.

DARREN: Yeah, the runup from June 2016 up.

MICHAEL: Got it.

DAN: That was just -- that was technical flows. That was -- money had to come out of certain instruments and go into government instruments or something. That caused 3-month LIBOR to decouple from 1-month LIBOR, and obviously twelve months went with it--six and twelve months went with it. That was the decoupling in that big, steep rise, and I want to say when it came off of that, which was November -- I don't know, where it says the high point. The high point down, that was just some normalization at the time. I didn't think it was fed, you know, Fed induced. I'll get -- I need to get more color. I need to get it -- I need to work with Marty on that. I don't -- I wouldn't sit here and say you

should just guarantee yourself every time the Fed raises 25, you're gonna have a 20-basis point contraction in the basis. I don't think that's the case.

DARREN: I don't think that's correct, either. To kind of stretch a point, well, that means the spread's going to go to zero in four rate moves.

DARREN: Yeah. There's a lot that goes on in the front end. Like when people say, "the front end to the curve", they typically say the two-year treasury, but now when you're getting into one month, one year, this is like -- they call this like, you know, cash. It's not even -- it's inside of the front end even, and there's a lot of dynamics, a lot of dynamics that I just never -- I never really had exposure to that caused this. It's like overnight repo, general collateral, Fed funds futures, OIS--all things that kind of cause gyrations, you know, kind of before fed, after fed, and it takes time for things to catch up. Now, again, the median for the one month, one year is the (U/I) point, so there's no getting around that, but I need

to get more color on what to expect going forward as a basis.

MICHAEL: Fifty basis points over what time period?
DARREN: The history.

MICHAEL: Hmm. So it looks like on this chart here it's 65, so it's artificially high from March 2014 till today so –

DARREN: On this chart we're at 82. Oh yeah, you mean the mean. The mean, yeah, this is just a short period of time. I think if you go back further -- the first chart I sent you, I don't know if –

DAN: I'm looking at it on Bloomberg, 2010 to 2017, the mean is 63.

DARREN: Yeah, almost 64.

MICHAEL: I'm sorry, over what time period, Dan?

DAN: 2010 to 2017, till today.

MICHAEL: Oh. How about, you know, forever?

DAN: Okay. Since 2000, it's 50, and -- let's see if I can go back further. Since 1990, 38.

MICHAEL: And the reason this is crushing us is because of the damn par floater that's being indexed to 1-month LIBOR as opposed to one year?

DARREN: Yeah.

DAN: Exactly right.

DARREN: Yes.

MICHAEL: Oh, man. All right, so it sounds like there's a long shot that we're gonna see this spread widen again by the 20 BPS that we just lost, but nonetheless, Dan, if you can show me scenario 1 and 2, were that to occur, what the resulting impact would be, so call it, you know, call it scenario 6 and 7, 6 being scenario 1, you know, plus 20 BPS added to the one month versus one year spread prospectively and the same thing for scenario 2. Again, not because I'm saying that's where we're gonna go; I'm just

trying to understand how much that spread matters for scenarios 1 and 2.

DAN: To be clear, we should use the exact spread deterioration, right, which I think –

MICHAEL: Right.

DAN: -- is not 20. It's something less than 20.

MICHAEL: Well, whatever it is. Yes.

DAN: Okay, so we're gonna -- I -- okay, so scenario 6 is we're gonna go find whatever the deterioration is, and then it's -- we're going to do what with that, and maybe I can work with Darren.

MICHAEL: Apply it to scenario 1. Everything else remains the same.

DAN: Well, if we do it scenario 1, then what's gonna change is just the percent Live Well prepay.

MICHAEL: I understand.

DAN: Okay, okay. Yeah. Okay. Okay. So -- okay, so scenario 1, we're gonna contract the basis, whatever it actually did, again.

MICHAEL: Yep.

DAN: Okay, and then scenario 7 is –

MICHAEL: Not contract; expand.

DAN: Or expand, expand, okay.

MICHAEL: Yeah.

DAN: Okay, and then what would scenario 7 be?

DARREN: Doing the same expansion of the basis spread of, you know, whatever it is. You know, we're using 20 BPS, but whatever the actual number is –-

DAN: Oh, so do the same thing except with scenario 2?

DARREN: Correct.

DAN: Okay. Okay, all right, so 6 is scenario 1, and we're gonna basically expand the

basis to whatever it actually did during which –

DARREN: Yeah.

DAN: Okay, for March. All right, then scenario 7 is whatever it actually expanded -- or whatever it actually contracted in March, we're going to expand it and use the pricings in scenario 2 to solve the percent level of prepay.

DARREN: Right.

MICHAEL: Again, I'm just trying to understand if spreads widen back to what they were before, you know, the world went haywire, you know, what that buys us in the form of slowing, or you know, speeding up, I guess, prepays, right? I'm trying to understand kind of that tradeoff between the two.

DARREN: Okay, and then, Eric, I'm gonna apply the liquidity to the last liquidity published to Michael.

ERIC: Yep.

DARREN: Yep. Okay.

ERIC: Just make sure, you know, because I know you and Annie have a little language about which scenario or whatever –

DARREN: Yeah. I have it.

ERIC: -- you've confirmed that with her. She knows the one we've reviewed with Michael.

DARREN: Yeah, understood. And is this -- is this, does this take place of this stuff that we talked about earlier regarding the rise in rates? Like is the deliverable only now 6 and 7 or is it now 6 and 7 plus analysis that we discussed earlier?

MICHAEL: The analysis we discussed earlier in terms of disentangling the impact of static versus basis, scenario 3, also needs to be done, but I would say I'm more interested in seeing scenario 6 and 7 first and having you send that out than I am seeing that.

DARREN: Okay.

MICHAEL: So scenario 6 and 7 should be priority one, analysis to disentangle for scenario 3. The impact of static versus basis compression would be priority two.

DARREN: Got it.

DAN: Eric, anything else you want to see scenario-wise?

ERIC: No, I think that would be good. I think that will lead to questions and insights --

DAN: Yeah.

ERIC: -- that may dictate if we go anywhere else, so –

DAN: Yep. Okay.

MICHAEL: All right. Thank you, guys. I appreciate it. I don’t have any further questions.

ERIC: All right.

[END OF RECORDING]